

Message Text

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ACTION ARA-20

INFO OCT-01 ISO-00 AID-20 CIAE-00 COME-00 EB-11 FRB-02

INR-10 NSAE-00 RSC-01 TRSE-00 XMB-07 OPIC-12 SP-03

CIEP-02 LAB-06 SIL-01 OMB-01 NSC-07 SS-20 STR-08

CEA-02 DRC-01 /135 W

----- 064539

P 282140Z MAY 74

FM AMEMBASSY LIMA

TO SECSTATE WASHDC PRIORITY 0234

C O N F I D E N T I A L SECTION 1 OF 2 LIMA 4120

E.O. 11652: GDS

TAGS: EGEN, ETRD, ENRG, BEXP, PE

SUBJECT: FINANCE MINISTER REVIEWS PERU'S ECONOMY, REJECTS
DEVALUATION

REFS: LIMA 4095, 4093, 1930, 1430, A-87

1. SUMMARY: IN BLAND TV APPEARANCE MAY 22, FINANCE MINISTER MARCO DEL PONT REPORTED TO NATION ON ECONOMIC RESULTS OF FIRST QUARTERS UNDER HIS STEWARDSHIP. HIS MOST FORTHRIGHT STATEMENT WAS TO DENY CATEGORICALLY THAT GOP WAS CONSIDERING DEVALUATION, BUT THE STATISTICAL ACHIEVEMENTS HE CITED FELL SOMEWHAT SHORT OF CONVICTION, AND HE FAILED EVEN TO MENTION IN THE BODY OF HIS ADDRESS THE NEW 180-DAY NEW IMPORT CREDIT REQUIREMENTS WHICH HAVE SOWN SO MUCH CONCERN IN THE BUSINESS COMMUNITY.

2. IN EMBASSY VIEW, IT DIFFICULT TO DETERMINE TO WHAT EXTENT THE MINISTER VIEWED HIS APPEARANCE AS ROUTINE OR AS AN EFFORT TO INSTILL CONFIDENCE BUT THERE IS NO DENYING THAT IT FELL SHORT ON BOTH COUNTS IN COMPARISON WITH PERFORMANCE OF HIS PREDECESSOR, GENERAL MORALES BERMUDEZ (WHO, WHILE BEING MORE EXPERIENCED, DYNAMIC, AND PERHAPS MORE ABLE, HAD THE GOOD FORTUNE TO TRANSFER COMMAND BEFORE THE INTERNATIONAL
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ECONOMIC STORM HAD BEGUN TO EFFECT PERU). IN ANY CASE, THERE

IS NO DOUBT THAT PERU IS FEELING EXTERNAL ECONOMIC PRESSURE AND THAT THE NEW IMPORT CREDIT REQUIREMENTS ARE INTERNALLY BEING VIEWED AS, IF NOT A SIGN OF PANIC, AT BEST A SIGN OF UNCERTAINTY. MINISTER MARCO DEL PONT'S SPEECH DID NOTHING TO QUELL DOUBTS. WE CONTINUE TO BELIEVE THAT PERU'S ECONOMY AND BALANCE OF PAYMENTS POSITION IS AS SOUND AS THAT OF MOST NATIONS IN THE HEMISPHERE AS THEY CONFRONT CURRENT INTERNATIONAL UNCERTAINTIES, AND WE AGREE WITH INFORM IBRD ASSESSMENT THAT DEVALUATION WOULD MAKE NO ECONOMIC (OR INDEED POLITICAL) SENSE. NEVERTHELESS, DESPITE MARCO DEL PONT'S SPEECH, DEVALUATION RUMORS ARE IN THE AIR AND WILL CONTINUE TO EFFECT SHORT-RUN BUSINESS DECISIONS. END SUMMARY.

3. GENERAL MARCO DEL PONT, MINISTER OF ECONOMY AND FINANCE, IN TV SPEECH, MAY 22, CATEGORICALLY DENIED RUMORS OF DEVALUATION WHICH HE SAID WERE BASED ON A COMPLETE LACK OF UNDERSTANDING OF THE ECONOMIC MEASURES THE GOP HAS UNDERTAKEN. IN 30-MINUTE SPEECH, FOLLOWED BY QUESTION AND ANSWER SESSION, THE MINISTER REVIEWED THE GOP'S BIENNIAL PLAN GOAL, THE 1973 ECONOMIC RECORD, AND MADE PREDICTIONS FOR 1974.

4. 1973 REVIEW - THE MINISTER ADMITTED IN AN OFF-HAND FASHION THAT REAL GDP GROWTH ROSE ONLY AT 5.8 PERCENT IN 1973, AND SAME RATE AS IN 1972, AND FAILED TO MEET PLANNED GOAL OF 7.2 PERCENT WHICH HE CLAIMED WAS DUE TO FISHMEAL SHORTFALL AND IMPORTED INFLATION (HE MADE NO MENTION OF THE EFFECT OF SLOW INDUSTRIAL GROWTH ON OVERALL GROWTH RATE.) THE BALANCE OF PAYMENTS REGISTERED A SURPLUS OF \$13 MILLION IN 1973 AND WAS HELPED ALONG BY A FAVORABLE TRADE BALANCE OF \$90 MILLION PLUS \$365 MILLION IN NET LONG TERM CAPITAL INFLOWS, MOSTLY IN RESPONSE TO DRAW-DOWNS ON PUBLIC SECTOR LOANS AND SOME DIRECT INVESTMENT IN MINING AND PETROLEUM. PERU CONTINUED TO BE PLAGUED BY A LARGE DEFICIT (\$303 MILLION) ON ITS SERVICES ACCOUNT. USING TECHNICALLY ACCURATE BUT AT BEST DISINGENUOUS STATISTICS, THE MINISTER SAID THAT THE ANNUAL RATE OF INFLATION IN 1973 AMOUNTED TO ONLY 9.5 PERCENT FOR THE "12-MONTH PERIOD." (TRUE, IF CALCULATED ON A MONTHLY AVERAGE FOR 1972 COMPARED TO THAT OF 1973, A GOOD GDP DEFLATOR, BUT MISLEADING TO THE PUBLIC

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WHICH IS ACCUSTOMED TO CALCULATING PRICE INCREASES ON A CALENDAR YEAR BASIS. THE GOP HAD PREVIOUSLY ANNOUNCED A PROVISIONAL 13.6 PERCENT INFLATION RATE FOR 1973 ON A CY BASIS, PROBABLY AT LEAST THREE POINTS UNDER THE ACTUAL RATE, THE EMBASSY ESTIMATES.) PRICE INCREASES WERE CAUSED BY SUBSTANTIALLY HIGHER COSTS FOR FOOD, VEGETABLE OILS, FERTILIZERS, INTERMEDIATE AND CAPITAL GOODS, ALTHOUGH THE MINISTER SAID MANY OF THESE COSTS WERE ABSORBED BY GOP

SUBSIDIES. ON DECEMBER 31, 1973, NET INTERNATIONAL RESERVES
STOOD AT \$411 MILLION.

5. 1974 PREDICTION - LOOKING AHEAD, THE MINISTER SPOKE OF A
DISEQUILIBRIUM WHICH HE DEFINED AS "INTERNATIONAL ECONOMIC
INSTABILITY" CAUSED BY HIGHER COSTS OF MOST IMPORTS, INCREASES
GENERATED BY THE ENERGY CRISIS AND "INTERNATIONAL SPECULATION."
HE PREDICTED A 6.5 PERCENT GDP GROWTH THIS YEAR FROM INCREASED
EXPORTS AND INCREASED EXPANSION OF DOMESTIC DEMAND. ESTIMATED
EXPORTS SHOULD

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TO SECSTATE WASHDC 235

C O N F I D E N T I A L SECTION 2 OF 2 LIMA 4120

REACH \$1.6 BILLION (UP 43 PERCENT), WITH
FISHMEAL CONSTITUTING 18 PERCENT OF THE TOTAL.
MINERALS MAY REACH \$805 MILLION (UP 12.5 PERCENT)
CONSTITUTING 54 PERCENT OF THE TOTAL. HE SAID
THERE ARE NUMEROUS EXOGENOUS FACTORS OVER WHICH
PERU HAS LITTLE CONTROL BUT THAT SIMULTANEOUSLY GOP
MEASURES TO CONTROL THE ECONOMY WILL HAVE A POSITIVE
EFFECT.

6. SENSITIVE ISSUE OF NEW CREDIT REQUIREMENTS WAS NOT
DISCUSSED DURING THE FORMAL PRESENTATION BY THE
MINISTER, BUT AROSE IN QUESTION AND ANSWER SESSION
FOLLOWING HIS SPEECH. ACCORDING TO OFFICIAL "EL
PERUANO" VERSION, THE MINISTER NOTED IN PASSING THAT THE

NEW CREDIT RESTRICTUIONS HAVE NOT BEEN UNDERTAKEN TO RESTRICT IMPORTS (SIC), BUT TO "CONTROL" IMPORTS IN A WAY WHICH PERMITS "THE MOST RATIONAL USE OF FOREIGN EXCHANGE." MEF DIRECTOR SUPERIOR LUIS GIULFO THEN ADDED THAT GOP WISHES TO ASSURE THAT FOREIGN EXCHANGE IS USED TO SATISFY ESSENTIAL CONSUMPTION NEEDS AND NOT TO BUY LUXURY GOODS. HOWEVER, WEEKLY MAGAZINE "OIGA" ALSO QUOTES GIULFO AS SAYING FURTHER THAT GOP HOPES THAT IMPORTERS WILL MAKE USE FO EXISTING LINES OF CREDIT NOT PRESENTLY BEING USED TO EXTENT DESIRED, SINCE
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MANY IMPORTERS PREFER TO BUY ON SIGHT TERMS WHICH CREATES EXCESSIVE PRESSURE ON THE SHORT-TERM BALANCE OF PAYMENTS. THE FOLLOWING DAY IN AREQUIPA COMMERCE MINISTER BARANDARIAN IN NEWS CONFERENCE ADMITTED AS MUCH, NOTING THAT NEW CREDIT RESTRICTIONS WERE UNDERTAKEN IN PART BECAUSE THE TOTAL OF \$800 MILLION ASSIGNED FOR THE WHOLE YEAR TO PRIVATE SECTOR IMPORTS HAD ALREADY BEEN USED UP DUE TO SPECULATIVE BUYING IN PROSPECT OF A DEVALUATION, AS WELL AS TO RISING PRICES. BARANDARIAN SAID, IN CONCILIATORY MANNER, THAT GOP READJUSTING ITS IMPORT MECHANISM IN THIS WAY WITH OBJECT OF SIMPLIFYING THE PROCESS AND TO MAKE SURE THAT ALL IMPORTS ARE GENUINE NECESSITIES FOR THE ECONOMY.

7. IN EMBARRASSING GAFF, ONE NEWSMAN ASKED INTERIOR MINISTER JIMENEZ DE LUCIO HOW HE JUSTIFIED HIS PREVIOUSLY ANNOUNCED FIGURE OF 11 PERCENT INDUSTRIAL GROWTH FOR 1973, SINCE MARCO DEL PONT'S FIGURE ONLY 7.5 PERCENT. JIMENEZ DE LUCIO RETORTED WEAKLY HIS FIGURE RELATED ONLY TO FIRMS UNDER JURISDICTION OF HIS MINISTRY WHICH HAS SUPPLIED STATISTICS DIRECTLY TO HIS MINISTRY.

8. COMMENT: THE FIGURES PRESENTED BY MARCO DEL PONT, VAGUE AS THEY WERE, CORRESPOND CLOSELY WITH CENTRAL BANK DATA THE EMBASSY HAD RECEIVED IN PARTIAL FORM. WITH THE RELATIVELY INELASTIC TAX SYSTEM AND CONSEQUENT GROWING GOVERNMENT DEFICIT, SUBSTANTIALLY INCREASED SHORT-TERM DEBT, AND ONLY A GENERAL IDEA OF TOTAL IMPORT COSTS (PROBABLY AT LEAST \$1.4 BILLION FOR CY 74), IT IS CLEAR THAT THE GOP HAS BEEN SHAKEN BY THE WORLD-WIDE INFLATION, HIGHER INTERNATIONAL INTEREST RATES, AND LACK OF DOMESTIC GROWTH. FURTHER, EVIDENCE POINTS TO THE FACT THAT THE PRIVATE SECTOR HAS BEEN STOCKPILING AS RAPIDLY AS POSSIBLE TO AVOID INFLATIONARY EFFECTS AND IN FEAR OF POTENTIAL DEVALUATION, SO THAT A MINI-RUN ON FOREIGN EXCHANGE RESERVES MAY WELL HAVE OCCURRED. WE UNDERSTAND FROM VERY RELIABLE SOURCE THAT NET INTERNATIONAL

RESERVES (GROSS RESERVES MINUS 12-MONTH LIABILITIES)
DROPPED FROM THE \$411 MILLION FIGURE AT END OF MARCH
WHICH REPRESENTS AN OVERALL BALANCE OF PAYMENTS DEFICIT
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OF \$169 MILLION. THIS DROP REPRESENTS NOT ONLY DEBT
AMORTIZATION, AND ROLL-OVER FOR DEBT FOR WHICH NEW

CREDIT HAS NOT YET BEEN DRAWN DOWN, BUT SUBSTANTIAL
INCREASES AS WELL FOR CURRENT ACCOUNT PAYMENTS.
THE MINISTER SAID THAT AS OF MAY 7 NET INTERNATIONAL
RESERVES STOOD AT \$424 MILLION, A RATHER IMPLAUSIBLE
TWO-MONTH INCREASE OF ALMOST \$200 MILLION.)

9. PERU IS FACING HEAVY PRESSURE ON ITS BALANCE OF
PAYMENTS FROM SEVERAL FRONTS, INCLUDING HIGH DEBT
SERVICE RATIO, SHORT-TERM REFINANCING, LACK OF
SUFFICIENT INTERNAL REVENUE TO COVER FOOD AND PETROLEUM
IMPORTS, AND INSUFFICIENT FOREIGN EXCHANGE LIQUIDITY
FOR IMPORTS, AS WELL AS LACK OF NEW PRIVATE INVESTMENT
AND SLOW AGRICULTURAL GROWTH. THESE PRESSURES LEAD TO
RUMORS OF DEVALUATION WHICH THE GOP HAS ATTEMPTED TO
CUT SHORT WITH THE NEW CREDIT RESTRICTION AND THE
MINISTER'S PUBLIC STATEMENT. HOWEVER, THE INDIRECT
MANNER BY WHICH THE NEW SRESTRICTIONS WERE PROMULGATED
AND THE PARTIAL AND UNCLEAR STATISTICS WILL PROBABLY
NOT SERVE SPECULATION ABOUT THE OTHER SERIOUS ECONOMIC
PROBLEMS WHICH PERU MAY BE FACING IN THE SHORT TERM.
THE NEW IMPORT CONTROLS WILL, TO BE SURE LESSEN
PRESSURE ON THE BALANCE OF PAYMENTS SOMEWHAT. HOWEVER,
FACED WITH SLOW INDUSTRIAL GROWTH AND RISING INFLATION,
IT IS CLEAR THAT THE GOP INTENDS TO PUT STABILITY
BEFORE ECONOMIC GROWTH AND IS WILLING TO SACRIFICE
SOME IMPORTS (AND POSSIBLY SOME SMALL PRIVATE SECTOR
BUSINESSES) TO MAINTAIN ITS GENERALLY GOOD INTERNATIONAL
CREDIT RATING. NONE OF THIS REFLECTS PARTICULARLY WELL
ON MARCO DEL PONT'S STEWARDSHIP OF THE ECONOMY (EVEN
THOUGH HIS PUBLIC DISCLAIMER IS BASICALLY VALID),
PARTICULARLY IN COMPARISON WITH HIS STRONG, DECISIVE
AND WELL-KNOWN PREDECESSOR, MORALES BERMUDEZ, WHO HAD
THE GOOD FORTUNE TO LEAVE THE FINANCE MINISTRY BEFORE
THE EFFECTS OF WORLD-WIDE INFLATION STRUCK PERU.

10. EMBASSY SUBMITTING SPEECH AND BACKGROUND DATA BY
AIRGRAM.

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Message Attributes

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